

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION
AT RICHMOND, AUGUST 14, 2003

COMMONWEALTH OF VIRGINIA, ex rel.
STATE CORPORATION COMMISSION,
Applicant,

v.

CASE NO. INS-2003-00024

RECIPROCAL OF AMERICA and
THE RECIPROCAL GROUP,
Respondents.

ORDER SCHEDULING HEARING ON APPLICATION

On April 30, 2003, the Deputy Receiver of Reciprocal of America and The Reciprocal Group (collectively “ROA”) filed with the State Corporation Commission (“Commission”) an Application for Orders Setting Hearing on Liquidation of Reciprocal of America and The Reciprocal Group, Establishing Response Dates, Ordering Liquidation, Approving Claims Bar Dates, and Related Matters (“Application”). Therein, the Deputy Receiver of ROA requested that the Commission take certain actions with regard to the receivership of ROA. Among other things, the Deputy Receiver of ROA requested that the Commission declare ROA to be insolvent, enter an Order of Liquidation, and permit the payment of certain workers’ compensation benefits.¹ The Deputy Receiver of ROA more specifically asserted that ROA was currently making a number of medical and recurring partial or total disability payments “to individuals entitled thereto under the workers’ compensation insurance policies.” The Deputy Receiver of ROA further advised that, as of the date of the filing of the Application, these payments averaged approximately \$3,000,000 each month. Such payments were alleged to be “generally essential to the daily sustenance of the recipients in this Commonwealth and in other

¹ Application at 2.

states.”² The Deputy Receiver of ROA proposed to continue making the aforementioned workers’ compensation payments until the payments can be made by the guaranty associations.³

On May 2, 2003, the Commission entered an Order Setting Hearing on Liquidation of Reciprocal of America and The Reciprocal Group, Establishing Response Date, and Related Matters (“Scheduling Order”). Therein, the Commission set the Liquidation Hearing for June 19, 2003, and scheduled a second hearing (“Other Matters Hearing”) for September 17, 2003.

On May 6, 2003, the Special Deputy Receivers (“SDRs”) of Doctors Insurance Reciprocal, Risk Retention Group (“RRG”), American National Lawyers Insurance Reciprocal, RRG, and The Reciprocal Alliance, RRG (collectively, the “Tennessee Companies”) filed Objections to Hearing Procedures Requested in Deputy Receiver’s Application for Orders Setting Hearing on Liquidation of Reciprocal of America and The Reciprocal Group, Establishing Response Dates, Ordering Liquidation, Approving Claims Bar Dates, and Related Matters (“Objections”). Therein, *inter alia*, the SDRs of the Tennessee Companies stated that they do not object in principle to the continuation of workers’ compensation insurance policy payments by the Deputy Receiver of ROA.⁴ The SDRs requested more specific information on the payments proposed to be continued prior to the Liquidation Hearing.⁵

The Deputy Receiver of ROA responded to the Objections in his Response of Deputy Receiver to Objections to Hearing Procedures, which was filed on May 13, 2003. Therein, the

² Application at 3.

³ Application at 8, 22.

⁴ Objections at 5.

⁵ Id.

Deputy Receiver of ROA filed additional information that described in some detail the types of payments made under the ROA workers' compensation insurance policies.⁶

On May 14, 2003, the Commission entered an Order Requiring Filing of Additional Information. The Commission directed the Deputy Receiver of ROA to file certain information, including what workers' compensation insurance benefits should continue to be paid and the reasons therefor.⁷

On May 27, 2003, the Deputy Receiver of ROA filed Information Submitted by the Deputy Receiver in Compliance with the Commission's May 14, 2003, Order ("Compliance Filing"). In the Compliance Filing, the Deputy Receiver stated his opinion that he was "authorized by the hardship provisions of the 'Final Order Appointing Receiver for Rehabilitation or Liquidation' entered by the Circuit Court of the City of Richmond in Case No. CH03-155 to exempt the workers' compensation [policy payments] from his directive imposing a moratorium on further claims payments under ROA's direct insurance policies."⁸ The Deputy Receiver stated his position that such payments should continue to be made by ROA "until they can be made by the Virginia Property and Casualty Insurance Guaranty Association and similar associations in other states."⁹

On June 9, 2003, the SDRs of the Tennessee Companies filed a Notice of Opposition to Deputy Receiver's Application for a Finding of Insolvency, Order of Liquidation, Continuation of Disability Payments, and the Cancellation of Direct Insurance Policies of Reciprocal of America and The Reciprocal Group Absent the Imposition of Certain Safeguards ("Notice").

⁶ See Response of Deputy Receiver to Objections to Hearing Procedures filed on May 13, 2003, at 13-15.

⁷ Order Requiring Filing of Additional Information at 4, fn. 7.

⁸ Compliance Filing at 9. The Deputy Receiver of ROA further claimed that § 38.2-1606 A 1 a(i) of the Code of Virginia "manifests a public policy in this Commonwealth to provide such payments without limitation, in preference of all other payments due under an insolvent insurer's direct insurance policies." See id.

⁹ Id.

The SDRs of the Tennessee Companies stated that they do not object to the Liquidation Order permitting continued payment by the Deputy Receiver of ROA of certain workers' compensation insurance policy benefits, conditioned on the Deputy Receiver of ROA entering into an agreement for reimbursement to the ROA estate by an affected guaranty association, such as is described in § 38.2-1509 B 3 of the Code of Virginia for amounts paid after the Order of Liquidation is entered until the guaranty association is in a position to begin making those payments.¹⁰

The Liquidation Hearing of ROA was held on June 19, 2003. At the hearing, Commissioner of Insurance and Deputy Receiver of ROA Alfred W. Gross described in more detail the workers' compensation insurance policy benefits that he proposed to continue making.¹¹ Commissioner Gross also stated that he would entertain entering into reimbursement agreements with the appropriate guaranty associations.¹²

On June 20, 2003, the Commission entered an Order of Liquidation with a Finding of Insolvency and Directing the Cancellation of Direct Insurance Policies, in which the Deputy Receiver was directed to liquidate ROA and TRG ("Liquidation Order"). The Commission found, *inter alia*, that the Deputy Receiver of ROA should continue making workers' compensation insurance policy payments as described in the Application, until such time as the payments are assumed by the applicable insurance guaranty associations.¹³ The Commission found such payments to be generally essential to the daily sustenance of the recipients in this Commonwealth and in other states. The Commission also indicated that the Deputy Receiver of

¹⁰ Notice at 7-8. If such a condition was not imposed on continued payments, the SDRs of the Tennessee Companies sought to have the Liquidation Order restrict such payments to only those that are indemnity payments or medical payments representing true hardships. Notice at 8.

¹¹ Transcript at 39-42, 52 and Exhibit 4.

¹² Transcript at 55. In fact, Commissioner Gross stated that he had directed his Special Deputy Receiver to pursue such agreements. Transcript at 70.

¹³ Liquidation Order at 2.

ROA should continue to pursue reimbursement agreements with the associations with respect to any such payments made by the Deputy Receiver of ROA for which a guaranty association is liable.¹⁴ The Deputy Receiver of ROA was specifically authorized to continue making such payments.¹⁵

On July 11, 2003, the Deputy Receiver of ROA filed an Application for Order Authorizing the Continuation of Workers' Compensation Disability Payments by Reciprocal of America and The Reciprocal Group for Workers' Compensation Claims Denied Coverage by State Guaranty Associations ("Denied Workers' Compensation Application"). Therein, the Deputy Receiver of ROA seeks a Commission Order authorizing the Deputy Receiver of ROA to continue payment of medical and recurring partial or total disability payments for workers' compensation claims that were assumed by ROA through assumption reinsurance, or similar transactions, and denied or likely to be denied coverage by the applicable state guaranty associations.¹⁶

The Deputy Receiver of ROA specifically asserts that the guaranty associations of the applicable states have refused, or likely will refuse, to make certain workers' compensation insurance policy payments for workers' compensation claims that ROA assumed from Self-Insured Trusts ("SITs") in Alabama, Arkansas, Kentucky, and Missouri and Group Self-Insurance Associations ("GSIAs") in Mississippi, North Carolina, Tennessee and Virginia (collectively referred to as the "Assumed Businesses") as a result of assumption reinsurance or similar transactions ("Assumed Claims").¹⁷ The Deputy Receiver of ROA notes that the

¹⁴ Id. at 2-3.

¹⁵ Id. at 3.

¹⁶ Denied Workers' Compensation Application at 1.

¹⁷ Such Assumed Claims and assets of the Assumed Businesses were purportedly assumed by ROA through merger agreements or different forms of assumption agreements ("Agreements"). Denied Workers' Compensation Application at 4.

Assumed Claims will likely not be paid, because the Assumed Businesses were not member insurers and/or the policies under which the claims arose were not ROA policies. These payments total approximately \$125,139 weekly.

The Deputy Receiver of ROA further asserts that the insureds of the Assumed Businesses are direct insureds of ROA and, due to the necessity for continued payment by the recipients thereof, requests authorization from the Commission to continue making such payments.¹⁸ The Deputy Receiver of ROA classifies the Agreements as “assumption reinsurance.”¹⁹ The Deputy Receiver of ROA asserts that the livelihood of many injured workers is dependent upon continued receipt of the payments and that a discontinuation of such payments would cause the recipients to suffer a substantial hardship.²⁰ The Deputy Receiver accordingly seeks an Order from the Commission authorizing the continued payment of workers’ compensation insurance policy claims assumed by ROA through assumption reinsurance or similar transactions and denied or likely to be denied coverage by the applicable state guaranty associations.²¹

On July 25, 2003, the SDRs of the Tennessee Companies filed Objections to ROA/TRG Deputy Receiver Continuing to Make Certain Workers’ Compensation Payments that Could be Paid from Alternative “Safety Net” Sources (“Objections to Denied Workers’ Compensation Application”). The SDRs of the Tennessee Companies contend that the case for payment of the Assumed Claims is weak here, and it is unfair to create a priority for these claimants, because such claimants may be able to turn to uninsured employers funds (e.g., the Virginia Uninsured Employers Fund), self-insured guaranty funds, bonds or other surety posted by uninsured employers, and recovery from the employer against which the workers’ compensation payment

¹⁸ Id.

¹⁹ Id. at 6-7.

²⁰ Id. at 9. The Deputy Receiver of ROA states that payments to approximately 450 injured workers are at stake. Id. at 10.

was awarded.²² The SDRs of the Tennessee Companies state that they are not opposed generally to the payment of “hardship” workers’ compensation claims that truly are “essential to the daily sustenance of the recipients.” They challenge the payment of non-“hardship” medical payments to health care professionals and institutions, such as hospitals, on the grounds that these payments represent “an unfair priority payment to persons or entities who are, in general, indistinguishable from the [Tennessee Companies’] insureds and third-party claimants.”²³

The SDRs of the Tennessee Companies request that (i) ROA/TRG be required to make good faith efforts to obtain coverage by the applicable state guaranty association(s) for, and to resist the denial by such association(s) of, the workers’ compensation claims in question, including legal action where necessary, and to report its efforts and the results of those efforts to the Commission and to any other party that has entered an appearance in this matter; (ii) the Commission hold a hearing at which ROA/TRG would bear the burden of proving that the SITs and GSIAAs in question were in fact “direct insureds” of ROA/TRG; (iii) if the Commission determines that the SITs and GSIAAs in question were in fact ROA/TRG “direct insureds,” ROA/TRG be required to prove which of the claims in question represent “hardship” claims that are truly “disability” claims “essential to the daily sustenance of the recipients” and that ROA/TRG be permitted to continue to pay only such “hardship” claims; (iv) sufficient time be given before the requested hearing to conduct reasonable discovery on the “direct insured” and “hardship” issues; (v) to the extent recipients of the workers’ compensation payments in question have access to “safety net” sources of payment, such as (1) the Virginia Uninsured Employers Fund or to a similar fund or mechanism in another state, (2) a bond or other surety posted by a self-insured employer, or (3) recovery from the employer against which the workers’

²¹ Id.

²² Objections to Denied Workers’ Compensation Application at 3.

compensation payments were awarded, a stay be issued prohibiting ROA/TRG from continuing to pay the workers' compensation claims in question until a final decision is made on the merits of the "direct insured" and "hardship" issues; (vi) the ROA/TRG Deputy Receiver be ordered to determine as soon as possible what such "safety net" payments exist in each affected state and to make arrangements for the workers' compensation claimants in question to seek immediate recovery in each state from that safety net, including the notification of those claimants of the availability of such payments; and (vii) the ROA/TRG Deputy Receiver be ordered to respond to the objections raised by the SDRs of the Tennessee Companies within 10 business days detailing ROA/TRG's efforts and progress (1) in securing guaranty fund payments for the former SIT and GSIA policyholders in question, (2) in obtaining alternate funding from "safety net" sources in applicable guaranty fund states, and (3) in obtaining reimbursement agreements with the applicable guaranty funds.²⁴

The SDRs of the Tennessee Companies request that the Commission stay the continuation of workers' compensation payments until the "direct insured" and "hardship" issues are resolved on their merits.²⁵ The SDRs of the Tennessee Companies also argue that the Deputy Receiver of ROA has failed to support the Denied Workers' Compensation Application legally and factually.²⁶

On August 8, 2003, the Deputy Receiver of ROA filed his Response to the Tennessee Receivers' Objections to ROA/TRG Deputy Receiver Continuing to Make Certain Worker's Compensation Payments that Could be Paid from Alternative "Safety Net" Sources ("Response to Objections"). Therein, the Deputy Receiver claims that he is pursuing systematically different

²³ Id. at 8.

²⁴ Id. at 11-12, 24-25.

²⁵ Id. at 15.

²⁶ Id. at 16-22.

resources (aside from receivership assets) for payment of the workers' compensation insurance policy benefits, including the so-called "Safety Net," but asserts that to prevent substantial hardship to the recipients, continuation of these payments by the Deputy Receiver of ROA is necessary. He claims again that the policyholders of the SITs and the GSIA's are "direct insureds" and a direct responsibility of ROA, and he submits that the method of case-by-case segregation suggested by the SDRs of the Tennessee Companies among the recipients of those deemed to constitute true "hardship" claims would be highly subjective and impermissibly discriminate among similarly situated creditors.²⁷ The Deputy Receiver of ROA further outlines his ongoing efforts to seek reimbursement from other sources for these claims and asserts that there are potential problems with some of the proposed "Safety Net" sources.²⁸ The Deputy Receiver of ROA continues to maintain that claimants of the SITs and the GSIA's are "direct insureds" of ROA, that such payments constitute "hardship" payments, and that the Deputy Receiver of ROA proposes continued payments as an "interim measure" until reimbursement or payment from other sources can be secured.²⁹ The Deputy Receiver of ROA concludes by seeking a Commission Order that authorizes him to continue workers' compensation insurance policy benefits for claims assumed by ROA through assumption reinsurance, or similar transactions, and denied or likely to be denied coverage by the applicable state guaranty associations.³⁰

There are several complicated issues that must be resolved that arise from the Denied Workers' Compensation Application. Such issues include, but are not limited to, whether the claimants of the SITs and GSIA's are entitled to be treated as "direct insureds" of ROA or, if not,

²⁷ Response to Objections at 6.

²⁸ Id. at 6-13.

²⁹ Id. at 13-20.

³⁰ Id. at 20.

whether the Assumed Claims constitute “hardship” claims. Until such issues are resolved, we deem it appropriate for the Deputy Receiver of ROA to continue making these payments. We make no determination at this time as to the merits of the arguments raised herein, but altering the treatment of the claimants of the SITs and GSIA’s prior to a determination of the merits of this case could cause unnecessary upheaval to the claimants and create at least as great a danger of creating an unlawful preference as continuing the payments. We hereby instruct the Deputy Receiver of ROA to continue to make every effort to secure payment or reimbursement by the applicable guaranty association, or to obtain payment or reimbursement from any alternative source available for the Assumed Claims. Finally, the Deputy Receiver of ROA should document his efforts in this regard and file such documentation with the Commission prior to a hearing being held in this matter.

Accordingly, IT IS ORDERED THAT:

(1) A hearing is scheduled to determine whether the insureds of the Assumed Businesses are direct insureds of ROA and therefore a direct responsibility of ROA or, if not, whether such insureds’ claims should be treated as “hardship” claims, on September 17, 2003, at the State Corporation Commission, Tyler Building, 2nd Floor Courtroom, 1300 East Main Street, Richmond, Virginia, such hearing to commence upon the conclusion of the Other Matters Hearing currently scheduled for the same date;

(2) Parties shall respond to written interrogatories or data requests within (7) calendar days after the receipt of the same. Except as so modified, discovery shall be in accordance with the Commission Rules of Practice and Procedure, except as they have been modified by our Order in Aid of Receivership entered on February 11, 2003; and

(3) This matter is continued.